MING HOLDINGS (M) SDN BHD

v.

SYED AZAHARI NOH SHAHABUDIN & ANOR

HIGH COURT MALAYA, PENANG
RK NATHAN J
[CIVIL SUIT NO: 22-263-1990]
13 NOVEMBER 2002

COMPANY LAW: *Loan - Security for loan facilities - Section 133(1) Companies Act 1965 - Transaction entered in violation of - Whether necessarily void and unenforceable - Companies Act 1965, s. 133(A)(3) - Whether plaintiff prevented from recovering value of security pledged*

It was the plaintiff's case that at the request of the first and second defendants, the plaintiff had deposited a certain amount of Palmco shares with the banks granting the loan facilities to the defendants. The plaintiff contended that it had loaned the said shares on the express and implied understanding that it were to be returned to the plaintiff. However the defendants breached the terms and conditions of their loan facilities and defaulted in loan repayments. Thus, the plaintiff's shares were force-sold by the banks at a loss to the plaintiff. The plaintiff claimed for loss and damages suffered against the defendants.

The defendants submitted that there was an agreement between both parties that 500,000 of the 3,158,959 special issue shares were to be considered shares sold to the plaintiff but held by the defendants on the plaintiff's behalf as the plaintiff was a non-Bumiputra company and in consideration thereof the plaintiff would deposit as security a part of its Palmco shares to the respective banks. The defendants averred that the taking up of the special issue shares was for the joint benefit of the plaintiff and the defendants and that the defendants held the 500,000 shares on behalf of the plaintiff who deposited its Palmco shares together with the special issue shares taken by the defendants as security for credit facilities advanced for purchase of the special issue shares.

The defendants contended that this was illegal and contrary to public policy as the special issue shares were offered solely to the benefit of Bumiputra and Bumiputra owned companies and the plaintiff nevertheless risked circumventing the mandatory requirement for issue of those shares. Hence, it should be considered void and the plaintiff should be precluded from making any claim on those shares.

Held:

[1] The plaintiff had discharged its burden of proof in respect of this case. When the plaintiff pledged its shares for the benefit of the defendants it is implied that the defendants would ensure that the shares would be returned to the plaintiff by the banks and that if the shares were lost, the defendants would compensate the plaintiff for any loss incurred thereby or would replace those shares. (p 258 b-c)

[2] The defendants did not adduce any documentary evidence to substantiate their assertion that there was an agreement made between the plaintiff and the defendants that 500,000 of the 3,158,159 special issue shares were to be considered as shares sold to the plaintiff but held by the defendants on the plaintiff's behalf. Further, the defendants failed to call Hooi Kee Sum, the financial controller of Palmco to support their allegation. The defendants merely relied on oral evidence to try and prove their case. Thus, the court held that there was no such illegal arrangement. (p 258 f-h)

[3] The plaintiff was not prevented from recovering the value of the security pledged pursuant to s. 133(A)(3) of the Companies Act 1965 ('the Act'), where it was provided that although the charge transactions breached s. 133(1) of the Act, there was no voidness or unenforceability attached to the loan. (p 260 f-g)

[Claim for loss and damages allowed; defendants to pay plaintiff value of pledged shares.]

Case(s) referred to:

Co-operative Central Bank Ltd (In Receivership) v. Feyen Development Sdn Bhd [1995] 4 CLJ 300 ***(refd)***

Stamford Holdings Sdn Bhd v. Kerajaan Negeri Johore & Ors [1998] 1 CLJ 960 ***(refd)***

Legislation referred to:

Companies Act 1965, s. 133A(1)(b), (3), E

Rules of the High Court 1980, O. 18 rr. 14(1), 19(1)(a)

For the plaintiff - Louis Van Buerle; M/s Cheong Wai Meng & Van Buerle
For the defendants - Surinder Singh; M/s Ong & Manecksha

[The defendants have appealed to the Court of Appeal vide Civil Appeal No: P-02-962-02.]

Reported by Suhainah Wahiduddin

JUDGMENT

RK Nathan J:

Facts

Between 1984-1985, the plaintiff's directors were Datuk Chan Woot Khoon, Chan Koi Koon and Chan Fook Koon. Between 1982-1989, the 1st defendant together with Datuk Haji Mohd Yusof Latiff (the 1st defendant in a similar suit 22-262-90 heard together with this suit) Datuk Chan Woot Khoon and Chan Kai Koon were the directors and shareholders of Palmco Holdings Berhad (Palmco), a public company listed at the main board of the Kuala Lumpur stock exchange. On or about 8 August 1984 Palmco had a rights issue of 53,010,000 new ordinary shares of RM1 each at a price of RM1 per share payable in full upon acceptance on or before 3pm on 8 August 1984 on the basis of three new ordinary shares for every five ordinary shares held on 25 June 1984. Under the Palmco rights issue exercise of 1984, the following were the entitlement of the defendants and their immediate family members/ companies.

TABLE 1

Name of shareholders	Number of shares registered as at 25.6.1984	Number of rights issue shares entitlement
1. Tuan Syed Azahari Bin Syed Noh Shahabudin	55,126	33,076
2. Syarikat Saffora Sdn Bhd	1,449,906	869,943
3. Syed Kamil Bin Syed Noh Shahabudin	428,688 16,000	257,212 9,600
4. Abrizah Abdullah	4,410,597	1,646,358

Palmco also had a Bumiputra special rights issue of 9,640,000 shares of RM1 each in September 1984. Out of the 9,640,000 Bumiputra special rights issue a total of 3,158,959 shares were allotted to the following persons at RM1 per share:

1) 1st defendant	278,328
2) Abrizah Bt Abdullah	2,275,225
3) 2nd defendant	605,406
	3,158,959

Sometime in August 1984, the 1st and 2nd defendants obtained term loans from various banks listed below to subscribe for the 3,158,959 special Bumiputra Palmco rights issue shares. The 1st and 2nd defendants pledged the said 3,158,959 shares to various banks as part of the security for their loans as follows:

TABLE 2

Name of Borrower	Name of Bank	Term Loan Amount (RM)	Number of Bumiputra rights issue shares pledged to bank	Number of Palmo shares pledged by Plaintiff to bank
Syed Azahari bin Noh Shahabudin	European Asian Kuala Lumpur	RM1,000,000	1,000,000	240,000
Syed Azahari bin Noh Shahabudin	United Malayan Banking Corporation Berhad Penang	RM1,000,000 (CABD)	1,000,000	250,000
Syarikat Saffora Sdn Bhd	Perwira Habib Butterworth	RM2,000,000	a) 278,328 b) 605,406 c) 275,225	1,215,000

The total entitlement of the 1st defendant, his wife Abrizah bte Abdullah and the 2nd defendant in the Bumiputra Palmco rights issue shares amounting to 3,158,959 shares were taken up and paid for from the loans obtained from the banks stated above in the table and all the 3,158,959 special Bumiputra Palmco rights issue shares were pledged to the banks for the 1st and 2nd defendants' loans. The total 3,158,959 special Bumiputra Palmco rights issue shares were forwarded by MIDF Consultany and Corporate Services Sdn Bhd to the banks directly on the instruction of the defendants as security for the defendants' loans.

In the meantime the plaintiff also pledged it's Palmco shares as part of the security to be provided to the various banks for banking facilities given by the banks to the 1st and 2nd defendants as follows.

TABLE 3

Particulars

Name of Borrower	Name of Bank	No. of palmco shares pledged to the said Banks by the Plaintiffs
a) Syed Azahari Bin Noh Shahabudin	European Asian Bank Kuala Lumpur	240,000
b) Syed Azahari Bin Noh Shahabudin	United Malayan Banking Berhad, Penang	250,000
c) Syarikat Saffora Sdn Bhd	Perwira Affin Bank Butterworth	1,215,000

The 1st and 2nd defendants defaulted in the loan repayments to the banks and as a result thereof the banks force-sold the plaintiff's and the defendants' Palmco shares and the proceeds thereof were utilised to repay the monies due by the 1st and 2nd defendants to the banks. The price of Palmco shares as at the date of filing of this suit ie, on 26 July 1990 was RM2.66 per share.

Plaintiff's Case

It is the plaintiff's case that some time between August to October 1984, the 1st and 2nd defendants requested the plaintiff to deposit the plaintiff's Palmco shares with the banks granting the loan facilities to the defendants and the plaintiff did accordingly deposit it's Palmco shares with the banks in the manner stated in table 3 above.

The plaintiff pleaded that it was *inter alia* a condition in the banks' letter of offer to the 1st and 2nd defendants respectively for the loan facilities that the plaintiff do execute a memorandum of deposit of its Palmco shares (MOD) as security for their respective loans. At the request of the 1st and 2nd defendants the plaintiff executed the MOD of 865,000 Palmco shares in favour of the banks on the terms and conditions stated in the MOD. Since the 1st and 2nd defendants breached their respective loan agreements with the respective banks the banks therefore force-sold the plaintiff's Palmco shares without the knowledge of the plaintiff. In the premises the plaintiff's Palmco shares were lost and the plaintiff claimed for the loss and damage suffered. Alternatively, it is the plaintiff's case that at the request of the 1st and 2nd defendants the plaintiff loaned a total of 865,000 Palmco shares to the 1st and 2nd defendants to enable them to obtain loan facilities from their bankers, particulars of the number of shares loaned to the 1st and 2nd defendants are as follows:

(a) 1st defendant 490,000 Palmco shares.

(b) 2nd defendant 1,215,000 Palmco shares.

At the request of the 1st and 2nd defendants the plaintiff delivered its Palmco shares to the defendants' bankers as security for loan facilities granted by the 1st and 2nd defendants' bankers to the 1st and 2nd defendants, the particulars of which are as stated in Table 3. The plaintiff contended that it had loaned the said Palmco shares to the defendants on the express and or implied understanding that the said shares were to be returned to the plaintiff by the defendants on demand. It was also an express and/or implied condition that the defendants would not breach the terms and conditions of their loan agreement with their respective banks so as not to jeopardize the plaintiff's shares deposited with the said banks. Since the defendants breached the terms and conditions of their loan facilities with their respective banks, the plaintiff's shares deposited with the said banks were force-sold by the banks at a loss to the plaintiff. The plaintiff therefore claimed as against each of the defendants as follows:

(a) as against the 1st defendant an order that the 1st defendant do forthwith return the 490,000 Palmco shares to the plaintiffs and

(b) alternatively the 1st defendant do pay the plaintiff the value of the 490,000 Palmco shares as at date of judgment.

(c) as against the 2nd defendant, an order that the 2nd defendant do forthwith return the 1,215,000 Palmco shares to the plaintiff.

(d) Alternatively that the 2nd defendant do pay the value of 1,215,000 Palmco shares as at the date of judgment.

(e) Damages as against both defendants.

(f) Interest.

(g) Costs.

Case For The Defendants

In their defence the defendants admitted accepting the 9,640,000 special issue shares for the benefit of Bumiputra or Bumiputra owned companies and also confirmed that the 1st defendant, his wife and the 2nd defendant together took up the 3,158,459 shares issued.

However, it was the contention of the defendants that it was agreed between the defendants and the plaintiff, several of whose directors were also directors of Palmco and several of whose shareholders were shareholders of Palmco that 500,000 of the 3,158,959 special issue shares were to be considered shares

sold to the plaintiff but held by the defendants on the plaintiff's behalf as the plaintiff was a non-Bumiputra company and in consideration thereof the plaintiff would deposit as security a part of it's Palmco shares to the respective banks together with the 3,158,959 special issue shares taken up by the defendants for credit facilities advanced by the respective banks to finance the purchase of the special issue shares. The defendants pleaded that the deposit of the plaintiff's Palmco shares with the respective banks was a commercial transaction supported by consideration.

It is the case of the defence that the agreement that 500,000 of the 3,158,959 special issue shares considered shares sold to the plaintiff but held by the defendants on the plaintiff's behalf as the plaintiff was a non-Bumiputra company and in consideration whereof the plaintiff would deposit as security a part of it's Palmco shares to the respective banks, was contrary to public policy, illegal and therefore void as the special issue shares were offered solely to the benefit of Bumiputra and Bumiputra owned companies and that this fact was known to the directors and shareholders of the plaintiff who nevertheless risked circumventing the mandatory requirement for issue of those shares. Further and in the alternative the defendants state that the 1st named defendant was at all material times a director of Palmco and so were three of the directors of the plaintiff and as such the plaintiff ought not to have provided any security to the several banks for loans made to the defendants as such provision of security is contrary to s. 133A(1)(b) of the Companies Act 1965 and is void. The defendants admitted that the respective banks had sold the shares pledged by them as security, including the shares belonging to the plaintiffs at the time of depression and where the price of each share dropped below par.

Further and in the alternative the defendants averred that the taking up of the special issue shares was for the joint benefit of the plaintiff and the defendants and that the defendants held the 500,000 shares on behalf of the plaintiff who deposited its Palmco shares, together with the special issue shares taken by the defendants as security for credit facilities advanced for purchase of the special issue shares.

The defendants therefore counterclaimed for a declaration that the deposit of the plaintiff's Palmco shares with the respective banks was contrary to public policy, illegal and void by reason of the fact that it was done to circumvent the issuance of shares to Bumiputra and Bumiputra Controlled Companies and for a further order that the plaintiff be precluded from making any claim on those shares.

Findings Of The Court

The defendants admitted that the plaintiff pledged its Palmco shares as part of the security to be provided to the various banks for banking facilities given

by the said banks to the defendants, particulars of the banks and the number of the shares pledged by the plaintiff are as stated in Table 3 above. The defendants also admitted that they defaulted in the loan repayment to their banks and as a result thereof, the banks force-sold the plaintiff's and the defendants' Palmco shares and the proceeds thereof were utilised to repay the monies due by the defendants to the banks.

It is my judgment that the plaintiff has discharged its burden of proof in respect of this case. When the plaintiff pledged its shares for the benefit of the defendants it is implied that the defendants would ensure that the shares would be returned to the plaintiff by the banks and that if the shares were lost, the defendants would compensate the plaintiff for any loss incurred thereby or would replace those shares.

What this court has to decide therefore is whether there was an agreement made between the plaintiff and the defendants that 500,000 of the 3,158,959 special issue shares were to be considered as shares sold to the plaintiff but held by the defendants on the plaintiff's behalf and that if there was indeed such an agreement, whether such an agreement is contrary to public policy and is therefore illegal and void and that in such circumstances whether the defendant ought to return to the plaintiff the Palmco shares force-sold by the banks or their value thereof. I have also to consider whether the security provided by the plaintiff to the several banks for loans made to the defendants is contrary to s. 133A(1)(b) of the Companies Act and is void.

It is in evidence that the defendants appealed to the Ministry of Trade and Industry (MITI) for the Bumiputra shares to be allocated to them instead of to Bumiputra institutions since they were unable to meet the immediate financing as required. It must be noted that the Bumiputra shares cannot be sold without MITI's approval. Only the 1st defendant gave evidence on behalf of the defendants. The defendants did not adduce any documentary evidence to substantiate their allegations. The 1st defendant's evidence was that the illegal arrangement made with the plaintiff was done orally. It is pertinent to note that defence counsel had put to PW1 that Hooi Kee Sum, the financial controller of Palmco had full knowledge of the illegal arrangement. This was denied by PW1. The defendants however failed to call Hooi Kee Sum to support their allegation nor have the defendants given any explanation as to why Hooi Ke Sum was not called as their witness. I am therefore compelled to hold, from the defendants' failure to call Hooi Kee Sum as their witness, that there was no such illegal arrangement. The defendants merely relied on oral evidence to try and prove their case. The defendants made serious allegations but were not able to sustain the said allegations by any documentary evidence. For example, the defendants' witness said that he could produce some account that would show the existence of a pool account. At the conclusion of the trial no such

account was produced. The defendants' witness also alleged that he advanced Datuk Chan some monies from the RM800,000 being the balance of his loan. He however admitted that he was unable to substantiate the same with any documentary evidence.

On the defendants' admission that they did not have the financial resources to take up their rights issue entitlement and the Bumiputra shares and the fact that the 1st defendant's wife Abrizah bte Abdullah did not take up her rights issue entitlement of 1,646,358 shares and coupled with the fact that the volume of the defendants' securities provided to the banks were insufficient, I find that under such circumstances the plaintiff had at the request of the defendants, pledged its shares to the bank to top up the difference so that the defendants could draw down on their loans.

The 1st defendant also testified that the defendants could have sold their rights in the Bumiputra shares and would have made a reasonable profit but chose to take up the Bumiputra shares because of their involvement in Palmco and because of their close relationship with the Chan family. I reject this viewpoint as not being credible. The 1st defendant is a businessman. He had admitted in evidence that the primary objective of the defendants in taking up the Bumiputra shares was the expectation of making a profit. In any case the Bumiputra directors and their families' and companies' shares totalled about 2% of the paid-up capital of Palmco as opposed to the Chan family's control of Palmco and the 1st defendant's sentimental inclination towards Palmco and the Chan family could have made no impact at all.

The 1st defendant was also unable to specify how much of the 500,000 Bumiputra shares were to be allotted by each defendant to the plaintiff especially when in their defence it was pleaded that the defendants and the 1st defendant's wife had jointly taken up 3,158,959 shares. This inability of the defendants to specify how much of the alleged 500,000 Bumiputra shares each was alloted to the plaintiff, further adds to the disbelief of the defence story. I therefore reject the defendant's evidence regarding the alleged 500,000 Bumiputra shares allotment to the plaintiff.

Section 133A Of The Companies Act 1965 (The Act)

The defendants contend that because of the provisions of s. 133A(1)(b) of the Act the loans advanced by the plaintiff to the defendants are illegal and any loan agreement must be rendered void. It is therefore necessary to reproduce s. 133A(1)(b) of the Act which reads as follows:

> Subject to the provisions of this section, a company (other than an exempt private company) shall not:

(a) xxx

(b) enter into any guarantee or provide any security in connection with a loan made to such person by any other person.

The plaintiff is a company wholly owned by the Chan family and is an exempt private company and besides, the 1st defendant is not a director of the plaintiff. In any case at the material time when the plaintiff pledged its shares for the benefit of the defendants, the Act had not been amended to include s. 133A as yet. The amendment to include s. 133A was made by way of gazette No. PU(B) 46/87 (A 657) which came into force on 1 February 1987 and accordingly s. 133A was not applicable at the time when the pledge was made. However, even if s. 133A(1)(b) applies the plaintiff is not prevented from recovering the value of the security pledged pursuant to s. 133A which reads as follows:

> Nothing in this section shall operate to prevent the company from recovering the amount of any loan or the amount for which it becomes liable under any guarantee entered into or in respect of any security provided in contravention of this section.

In *Co-operative Central Bank Ltd (In Receivership) v. Feyen Development Sdn Bhd* [1995] 4 CLJ 300 FC the Federal Court held that there is a general rule that where a contract is prohibited by statute expressly or by implication and the statute stipulates for penalties for those entering into it, the contract shall be void and unenforceable, unless saved by the statute itself or there are contrary intentions which can reasonably be read from the statute. Relating to s. 133E of the Act, the Federal Court went on to hold that s. 133 does not state that a guarantee entered into or any security given in contravention thereof is to be void, although criminal liability would be imposed on the official of the company and on the company itself. The Federal Court referred to s. 133(5) of the Act which is almost in identical terms to s. 133A(3) of the Act and held that no voidness or unenforceability attached to the loan or the charges although the charge transactions breached s. 133(1) of the Act.

Return Of 100,000 Palmco Shares

The 1st defendant testified that he had returned 100,000 Palmco shares to the plaintiff through one Teoh Kah Tin. To my mind this is irrefutable evidence that it was the intention of the parties that the plaintiff s pledged shares were to have been returned to the plaintiff.

In any case the plaintiff submits that at the time when the shares were returned to Teoh Kah Tin he was not a director of the plaintiff and the plaintiff was not aware of the return of the shares. However in his submission counsel for the plaintiff has stated that he has instructions to acknowledge the return of

the 100,000 shares and therefore he asks that a sum of 50,000 shares each be deducted from the amounts claimed from the defendants.

Since the banks have already force-sold the pledged shares it is my judgment that

1) the 1st defendant do pay the plaintiff the value of 440,000 shares.

2) The 2nd defendant do pay the plaintiff the value of 1,165,000 shares.

3) that the senior assistant registrar do hear argument as to what rate per Palmco share is to be fixed for the purposes of calculating the total value of the shares.

4) interest on the calculated value to run from the date of the order of the learned senior assistant registrar.

5) Costs.

I am not satisfied that the plaintiff has sufficiently shown that it had suffered any damages as a result of the force-sale by the bank. In any case the rate to be fixed per Palmco share by the learned senior assistant registrar after hearing arguments would be sufficient to cater for any loss sustained.

Counter Claim

The defendant counterclaimed for:

(a) a declaration that the deposit of the plaintiff's Palmco shares with the respective banks is contrary to public policy, illegal and void by reason of the fact that it was done to circumvent the issuance of shares to Bumiputra and Bumiputra controlled companies;

(b) an order that the plaintiffs are precluded from making any claim on those shares.

(c) costs.

There was no reply nor defence to the counterclaim, filed by the plaintiff. The defendant contends that the counterclaim remains unanswered and is not denied. Since the counterclaim stated as a fact that there was an oral agreement of 500,000 promised to the plaintiff in return, and since this has not been traversed it is the defendants' view that it is deemed that the plaintiff has agreed that the allegations contained in the counterclaim are correct and true. For these reasons, the defendants prayed that the plaintiff s claim ought to be dismissed with costs.

In support the defendants' relied on *Stamford Holdings Sdn Bhd v. Kerajaan Negeri Johore & Ors* [1998] 1 CLJ 960. This was an appeal against the order of the High Court wherein the appellant's statement of claim against all the respondents was struck out under O. 18 r. 19(1)(a) of the Rules of the High Court 1980 (the RHC). It was the case of the appellant that since the defence had not been filed the contents of the statement of claim could be assumed to be true. The Court of Appeal held that it would assume that the contents of the statement of claim to be true in the absence of a defence being filed by the respondents. The court went on to hold that the facts as stated in the statement of claim clearly showed the unconscionable or unmeritorious conduct of the respondents. At least those facts, in the absence of any defence filed, ought to be assumed as true and stood unrebutted and would constitute a good cause of action against the respondents.

I do not accept that the decision in *Stamford (supra)* ought to apply to the case before me. What the defendants have done in this case is to present their version of the case which is contrary to the case presented by the plaintiff in its statement of claim. Order 18 r. 14(1) of the RHC reads that if there is no reply to a defence then there is an implied joinder of issues on that defence. Now the counterclaim of the defence is nothing new. It is in fact a repetition of the defence and relies on matters pleaded in the defence. In fact counsel for the defendants had conceded that this is so in his submission. What the defendants had done is to ask for a declaration that the deposit of the plaintiff's Palmco shares with the banker is contrary to public policy and to circumvent the issuance of shares to Bumiputra and to Bumiputra controlled companies. This is nothing new from what has been pleaded in the defence. In other words the counterclaim is not independent of the defence.

In any event the matter proceeded to full trial. The first witness for the plaintiff was thoroughly cross-examined based on the defence and on the counterclaim and there has been no element of surprise that the defendants had to face. I therefore dismiss the counterclaim but make no order as to costs on the counterclaim issue only.

Parties by consent had agreed that the decision in 22-262-90 would follow the outcome of this case as the plaintiff is the same and the defendants are in a similar factual situation as the defendants in this case. The parties are therefore directed to draw up the order in 22-262-90 as the order made in this case.